IN THE SUPREME COURT OF THE STATE OF MONTANA

NO. DA 08-0016

RANDALL G. KNOWLES, Appellee and Petitioner, v. STATE OF MONTANA, ex rel. JOHN M.MORRISON, Montana State Auditor and Ex-officio Commissioner of Securities, Appellant and Respondent.	

BRIEF OF APPELLANT

On Appeal from the Montana Eighth Judicial District Court, Cascade County
The Honorable Julie Macek, Presiding

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STATEMENT OF THE ISSUES

1. Whether the district court erred and abused its discretion by reversing the Montana Securities Department's (Department) final agency decision when that reversal is not supported by the reliable, probative and substantial evidence found in a review of the record in its entirety.

2. Whether the district court erred and abused its discretion by failing to give the legally required deference to the Department's interpretation of the rules and laws the Department administers.

STATEMENT OF THE CASE

On August 30, 2004, the Montana State Auditor's Securities Department (hereafter "Department") issued a Notice of Proposed Agency Disciplinary Action and Opportunity for Hearing and a Temporary Cease and Desist Order and Order Denying Application barring Petititoner/Appellee Randall G. Knowles (hereafter "Knowles") from conducting securities business in Montana on the basis of alleged wrongdoing in the accounts of certain Montana investors, including dishonest and unethical behavior and fraud. Knowles timely requested a hearing.

A hearing on the merits was held on March 21, 22, and 23, 2005, and Knowles' expert testified on April 29, 2005. The parties timely submitted post hearing briefs and proposed findings and conclusions to the hearing examiner. The hearing examiner issued her proposed Findings of Fact, Conclusions of Law and

Order on December 15, 2005. The parties filed exceptions and objections with the Ex-officio Commissioner of Securities John Morrison (hereafter "Commissioner") pursuant to Title 2, Chapter 4, Part 6, MCA. The Commissioner issued the final agency decision on May 23, 2006, and a corrected version was issued May 24, 2006.

Knowles filed his petition for judicial review pursuant to § 2-4-702, MCA in the Eighth Judicial District Court for Cascade County on July 24, 2006. Following the briefing schedule and presentation of oral arguments, Judge Macek issued her Order Reversing the Corrected Findings of Fact, Conclusions of Law, and Order of State Auditor, Ex-officio Commissioner of Securities on August 9, 2007. On September 25, 2007, the Department filed a Motion to Alter or Amend Order Pursuant to Rule 59 (g) tolling the statute of limitations regarding appeals to the Supreme Court. The Department alleged in its motion that the lower court had committed various errors of law, including an incomplete review of the findings of fact and inappropriate additions to the findings that resulted in the court reaching different conclusions and ultimately the court reversing the final agency decision. After submission of briefs, Judge Macek issued her Order denying the Department's Motion to Alter or Amend on November 15, 2007. Knowles filed his Notice of Entry of Judgment on November 29, 2007.

The Department then filed its Notice of Appeal on January 11, 2008.

STATEMENT OF THE FACTS

Persons working in the securities industry in a manner that affects investors' money and investments are required to take and pass specific exams, obtain continuing education and maintain proper registration to ensure persons of good character are employed in Montana's securities industry. (Hearing Tr. at 30:22-25; 31:1-21.) ***SEC v. Capital Gains Research, Inc.,*** 375 US 180 (1963). Additionally, these people must be registered prior to transacting securities business. (Hearing Tr. at 28:21-25; 29:1-22.) Persons working in the securities industry in a manner that affects investor's money and investments can only be registered if and when they are sponsored by a broker-dealer or investment advisor firm. (Hearing Tr. at 409:12-16.) Registration of these persons is required to protect investors. (Hearing Tr. at 30:11-21, 32:2-11.)

When securities transactions are made because the customer came to the securities salesperson with the idea for the transaction, the transaction would be marked on the trade ticket, confirmation notice and/or account statement as "unsolicited." (Hearing Tr. at 54:15-20; 59:19-25; 60:1-4.) When transactions are solicited (proposed to the customer by the securities salesperson), those transactions must be reviewed for suitability prior to effecting the transaction. (Hearing Tr. at 50:25; 51:1-11.)

Randall Knowles worked and was properly registered to work in the securities industry for approximately 18 years. (Hearing Tr. at 310:12-14.) While Knowles was duly registered to conduct securities business in Montana, he worked with a licensed insurance producer named Mark Payton in a scheme where Payton made contact with Montana senior citizens in order to sell them various annuity products issued by an insurance company. (Hearing Tr. at 271:20-25; 272:1-5.) As part of the scheme, Payton exclusively carried FSC Securities Corporation (FSC) brokerage forms provided to him by Knowles. (Hearing Tr. at 272:8-14; 274:10-25; 275:1-11.) If the senior citizen needed to liquidate securities they owned to purchase the annuity product, Payton would contact Knowles by telephone and Knowles advised Payton on procedures to move the securities to Knowles' management so Knowles could sell the securities. (Hearing Tr. at 283:3-25; 284:1-3.) The senior citizens involved in this matter ranged in ages from 68 to 81 at the time of their contact with Payton and Knowles. (Hearing Ex. K admt. at 353:9-25; 354:1-6[1]; Hearing Ex. 5 admt. at 64:8-19; 274:10-25; 275:1-2; Hearing Ex. F admt. at 331:16-25; 332; 333; 334:1-6.) Payton was never registered to conduct securities business in Montana and had no experience in the industry. (Hearing Tr. at 266:23-25; 267:1-6.)

[1] Due to the poor quality of the recording of this hearing, much of the testimony is transcribed as "inaudible," but appellant's counsel certifies that this exhibit was duly offered and admitted.

The Department received a letter in October 2002 from an investor from Hamilton, Montana. (Hearing Tr. at 41:1-4.) In her letter, Grace Simmons indicated Payton transferred Simmons' investments to Knowles' management and then Knowles sold those investments. (Hearing Tr. at 41:10-20.) Knowles dictated to Payton what information and materials to gather to effect a securities transaction for Simmons. (Hearing Tr. at 342:23-25; 343:1-18.) Knowles did not conduct a suitability analysis for the trades he effected for Simmons that were not marked "unsolicited" on the trade tickets or account statement. (Hearing Tr. at 48:5-20; 51:19-21.)

The sales of Simmons' investments were unsuitable because they resulted in negative tax consequences. Additionally, the proceeds from the sales were placed in a fixed annuity product that had substantial surrender penalties over a lengthy hold period, making it an unsuitable investment for Simmons. (Hearing Tr. at 221:22-25; 222:1.) Simmons was 81 years of age at the time of these transactions. (Hearing Tr. at 221:23-24; Hearing Ex. K admt. at 353:9-25; 354:1-6.[2])

Emily Downey, an investor from Butte, Montana, spoke with the Department on at least two separate occasions regarding her investments with Knowles. (Hearing Tr. at 44:17-25; 45:1-3.) Downey indicated Payton came to her home in early 2002 and reviewed her investments held at D. A. Davidson &

[2] See previous footnote re: inaudible parts of hearing recording.

Co. (Hearing Tr. at 131:3-9; 132:21-23; 136:14-23; 137:4-12.) Downey indicated Payton then got on the telephone while at her home and spoke with Knowles. (Hearing Tr. at 145:1-7.) Payton provided the forms for Downey to sign transferring her securities from her D.A. Davidson & Co. account to Knowles' management. (Hearing Tr. at 132:9-12; 132:21-23; 145:19-25; 146:1-23; Hearing Ex. 3 admt. at 146:24-25; 147:1-4; Hearing Ex. A admt. at 150:8-14; Hearing Ex. B admt. at 153:22-25; 154:1-16; Hearing Ex. C admt. at 155:20-25;156:1-4; Hearing Ex. D admt. at 157:2-10; Hearing Ex. P admt. at 157: 376:23-25; 137:1-15; Hearing Exs. Q and R admt. at 378:21-25, 379:1-23.[3]) Knowles dictated to Payton what information and materials to gather to effect a securities transaction for Downey. (Hearing Tr. at 375:6-25; 376:1-22.) Payton and Knowles effected the transfer of her investments to Knowles' management and Knowles subsequently sold approximately $79,000 in securities from Downey's IRA. (Hearing Tr. at 132:9-12; 132:21-23; 145:19-25; 146:1-23; Hearing Ex. 3, A, B, C, D, P, Q, R.) Knowles did not conduct a suitability analysis for the trades he effected for Downey that were not marked "unsolicited" on the trade tickets or account statement. (Hearing Tr. at 48:5-20; 51:19-21.)

The sales of Downey's investments were unsuitable because they resulted in negative tax consequences. Additionally, the proceeds from the sales were placed

[3] See previous footnote re: poor quality of hearing recording.

in a fixed annuity product that had substantial surrender penalties over a lengthy hold period, making it an unsuitable investment for Downey. (Hearing Tr. at 221:22-25; 222:1.) Downey was 68 years of age at the time of these transactions. (Hearing Ex. 3.)

Doris Haaland an investor from Missoula spoke with the Department in 2004. (Hearing Tr. at 45:10-16.) Haaland indicated Payton came to her home in early 2002 and reviewed her investments held at D. A. Davidson & Co. (Haaland Dep. Tr. at 6:4-19; 9:5-25.) Haaland indicated Payton then got on the telephone while at her home and spoke with Knowles. (Haaland Dep. Tr. at 9:21-25; 10:1-3.) Knowles dictated to Payton what information and materials to gather to effect a securities transaction for Haaland. (Hearing Tr. at 331:5-11.) Payton and Knowles transferred her investments to Knowles' management and Knowles subsequently liquidated approximately $11,355 of her securities. (Haaland Dep. Tr. at 12:2-9; Haaland Dep. Ex. 1 admt. Haaland Dep. Tr. at 24:1-4.) Knowles did not conduct a suitability analysis for the trades he effected for Haaland that were not marked "unsolicited" on the trade tickets or account statement. (Hearing Tr. at 48:5-20; 51:19-21.)

The sales of Haaland's investments were unsuitable because they resulted in negative tax consequences. Additionally, the proceeds from the sales were placed in a fixed annuity product that had substantial surrender penalties over a lengthy

hold period, making it an unsuitable investment for Haaland. (Hearing Tr. at 221:8-25; 222:1.) Haaland was 71 years of age at the time of these transactions. (Haaland Dep. Ex. 1.)

Knowles was allowed to leave his employment with FSC at the end of May 2004 due to "multiple problems" the company had experienced with Knowles' work including the appearance that he was "falsifying claim records." (Hearing Tr. at 224:2-20.) Knowles' registration as a securities salesperson terminated on the same day he ended his employment with FSC due to his loss of a broker-dealer firm's authority to act. (Hearing Tr. at 409:12-25; 410:8-23.)

Knowles applied for registration as a securities salesperson for the broker-dealer firm Signal Securities, Inc. on or about August 24, 2004. Knowles' application was denied by Order of the Commissioner along with the Temporary Cease and Desist Order issued on or about August 30, 2004.

On or about October 30, 2004, Knowles went to the home of Kaye Johnson, an investor in Great Falls, for the purpose of conducting business as a securities salesperson. (Hearing Tr. at 179:7-21; 180:1-25; 181:1-21; 182:8-12; 185:2-25; 186:1-20.) At this time Knowles' securities registrations had been terminated and his applications for new registrations had been denied by the Department.

Knowles and Johnson had a long-term investing relationship. (Hearing Tr. at 177:15-25; 178:1-10.) Knowles managed Johnson's securities accounts while he

worked for FSC and Rocky Mountain Investment Advisers. (Hearing Tr. at 47:3-6; 177:15-25; 178:1-10; 523:23-25; 524:1-3.) The relationship began a number of years prior to this action and included Knowles coming to the Johnson home to perform portfolio reviews. (Hearing Tr. at 177:15-25; 178:1-25; 182:8-17.) Knowles' appearance at the Johnson home in October of 2004 was no different than the numerous other times he had met with Johnson while acting as her properly registered securities salesperson and investment advisor representative. (Hearing Tr. at 182:8-17.)

While in her Great Falls home, Knowles accepted a check from Johnson for $3,500 to invest in her retirement account. (Hearing Tr. at 181:6-13; Hearing Ex. 6 admt. at 237:8-10[4].) Additionally, while meeting with Johnson, Knowles recommended Johnson invest some of her funds in the Franklin AGE High Income Fund. (Hearing Tr. 180:18-23.) Knowles subsequently referred the sale to her broker-dealer firm, FSC. (Hearing Ex. 6.) Knowles' letter to Eric Rolshoven at FSC Securities Corporation, dated November 4, 2004, indicates an attempt to effect the sale of the mutual fund shares for Johnson. (Hearing Tr. at 49: 12-25; 252:3-15.) Both the Department's expert, Lynne Egan, and Knowles' former supervisor, Eric Rolshoven of FSC, testified that these actions by Knowles with

[4] See previous footnote re: poor quality of hearing recording.

regard to Johnson constituted an attempt to effect a securities transaction. (Hearing Tr. at 49:15-24; 252:3-15.)

Knowles did not inform Johnson that he was no longer properly licensed to conduct business as a securities salesperson while he was at her home in October 2004. (Hearing Tr. at 181:2-5.) Nor did he inform her he was no longer properly licensed to conduct such business in his follow-up letter to Johnson dated November 8, 2004. (Hearing Ex. E admt. at 189:11-25; 190:1-4.)

Additional facts will be discussed as necessary in the argument below.

SUMMARY OF THE ARGUMENT

The Department maintains the lower court abused its discretion in its order reversing the Commissioner's final agency decision. The error was committed due to the court's incomplete reviewing of the record and inappropriate changing of the findings of fact. The court then compounded that error by failing to conduct the proper review that gives deference to the Department's weighting of the facts and evidence. Additionally, the lower court failed to give deference to the Department's expertise in the enforcement and interpretation of the laws and rules the Department administers. Had the district court conducted the proper review of the administrative record, refrained from substituting its judgment with regard to the evidence and given due deference to the Department's expertise in the

regulation of the securities industry in Montana, the Commissioner's Order would have been upheld.

ARGUMENT

I. A REVIEW OF THE ENTIRE RECORD FOR THE CONTESTED CASE HEARING INDICATES THE LOWER COURT'S ORDER REVERSING THE COMMISSIONER'S FINAL AGENCY DECISION WAS ERROR AND AN ABUSE OF THE COURT'S DISCRETION.

There is reliable, probative and substantial evidence on the whole record supporting the Commissioner's findings, inferences, conclusions and decisions, thereby preventing the lower court from reversing the Commissioner's decision as "clearly erroneous."

A. Standard of Review

A district court's reversal of an administrative agency's final decision because the decision is "clearly erroneous" is reviewed to determine whether the agency findings were clearly erroneous and whether the agency's conclusions of law were correct. § 2-4-704 (2) (a) (v), MCA; ***Key West, Inc. v. Winkler***, 2004 MT 186, & 13, 322 Mont. 184, 95 P.3d 666.

In determining whether findings of fact are "clearly erroneous" this Court relies on a three part test: (1) the record is reviewed for substantial evidence supporting the findings, (2) if the findings are so supported, the Court will determine whether that evidence was misapprehended by the agency, and (3) if the

evidence is supported by substantial evidence and it has not been misapprehended, the Court may still determine the findings are clearly erroneous if the review of the record leaves the Court with a definite and firm conviction that a mistake was made. ***Benjamin v. Anderson***, 2005 MT 123, & 31, 327 Mont. 173, 112 P.3d 1039.

However, the "substantial evidence" standard is not whether there is evidence to support findings of fact that are different from the hearing examiner's findings, but whether substantial credible evidence supports the examiner's findings as the trier of fact. ***Brackman v. Board of Nursing*** (1993), 258 Mont. 200, 205-206, 851 P.2d 1055, 1058. Also, because the hearing examiner is in the unique position of being present to observe the testimony his or her findings are entitled to a great deal of deference. ***Id.*** Finally, substantial evidence means more than a mere scintilla of evidence, but less than a preponderance of evidence. ***Schmidt v. Cook***, 2005 MT 53, 326 Mont. 202, 108 P.3d 511.

B. Discussion

In our case, the lower court begins its *de novo* review by indicating it was reviewing only a conclusion of law. However, findings of fact are changed by the court thereby allowing the court to support its decision that certain of the Commissioner's conclusions of law and his final decision were "clearly erroneous."

The lower court found that "Payton did not actually effect or attempt to effect the sales of securities." (Dis. Ct. Order at 20.) This specific finding by the lower court is in error. The products Payton were selling are not securities but are, instead, fixed annuities. The Montana Securities Act clearly articulates in § 30-10-103(22)(b), MCA, that the definition of a security "does not include an insurance or endowment policy or annuity contract under which an insurance company promises to pay a fixed sum of money either in a lump sum or periodically for life or some other specific period. Furthermore, the court made no specific cite to the record to support this finding.

Later in its order the court quotes the Commissioner's findings that "these securities transactions were solicited by Payton as an emissary of Knowles and that a suitability analysis was required." (Dis. Ct. Order at 22.) Then the court indicates "a review of the record does not support this finding." (Dis. Ct. Order at 22.) Again the court makes no specific reference to the actual record. Next, without citation to the record, the district court indicates "the record is clear and unrefuted that the clients initiated contact with Payton seeking information regarding securities." (Dis. Ct. Order at 22.) Finally, without citation to the record, the court indicates "[n]either Payton nor Knowles solicited the sale of a security." (Dis. Ct. Order at 22.) These findings by the lower court are in error and represent abuses of the court's discretion in reviewing the record.

A review of the entire record reveals a great weight of evidence supporting the Commissioner's findings with regard to Payton's role as Knowles' emissary and consequent solicitation of the Montana investors that are the basis of the allegations brought against Knowles. The administrative record includes the following reliable, probative and substantial testimony that Payton and Knowles worked together to solicit the securities transactions in question here - the liquidations of certain securities held by investors Emily Downey and Grace Simmons.

i. Payton's Actions as Knowles' Emissary

During the hearing examiner's cross-examination of Downey, the hearing examiner asked Downey how she knew Payton. (Hearing Tr. at 147:19-22.) Downey responded, "He said I sent in a card . . ." (Hearing Tr. at 147:23.)

Because Doris Haaland was deceased by the time this matter was heard, the Department relied on her video-taped deposition taken during its prosecution of Payton in Missoula on September 16, 2004. In that deposition, the Department's legal counsel asked Haaland how she met Payton. Transcript at 6:7. Haaland replied, "I sent a card to AARP to ask for information about their annuities." (Haaland Dep. Tr. at 6:8-9.)

Unfortunately Grace Simmons was unable to hear and/or understand the questions asked of her during the administrative hearing of this matter and gave

little testimony of value. However, Payton himself indicated in his testimony that the insurance company with which he was appointed to sell annuities created leads for him, ". . . they would mail out to people, and people would respond back sending in a card requesting for information about" the product he sold. (Hearing Tr. at 268:16-18.)

The testimony outlined above shows clearly that a third-party service contacted these seniors for Payton. Contrary to the lower court's Order, Knowles' victims did not contact either Payton or Knowles seeking to have Knowles liquidate their securities portfolios. (Dis. Ct. Order at 22.) Knowles used his securities license to effect the liquidation of the victims' securities portfolios after Payton made the initial contact and collected the information to effect the liquidations, as evidenced by the following testimony from Payton:

Q. When you went to these homes of your various contacts, did you carry with you Randy Knowles' securities forms?

A. Yes.

(Hearing Tr. at 272:8-14.)

Q. How did [the personal financial information] form get filled out?

A. I filled it out in the client's home.

Q. How did you get the information?

A. By questioning and answering with the client.

(Hearing Tr. at 274:14-18.)

A. . . . so I would call Randy who is security licensed, and tell him, "I'm in the client's home, and that they have a desire to something of that nature [sell securities to purchase the annuity product Payton was selling]," and then Randy would ask me what kind of securities does she have, and then he would advise me what paperwork that I needed to have signed and filled out while I was in the home.

(Hearing Tr. at 283:5-12.)

Knowles also provided direct testimony regarding Payton's collection of information for Knowles' use to liquidate the investors' portfolios:

Q. And did you have Mr. Payton gather information for you with regard to Doris [Haaland]?

A. Mark would have gathered the statements and he would have recorded the information on the confidential personnel (sic) financial planning form, and he would have also secured a copy of the trust documents.

(Hearing Tr. at 331:5-11.)

A. Well, again, I told Mark what information I would need [with regard to Grace Simmons], which would be a copy of all the statements involved, and that we needed to complete the confidential customer information form; possibly if there's three accounts involved, we might need three ACAT forms. And I'm not sure what other documents we may have—new account form with FSC, so if appropriate, we could open up an FSC account.

(Hearing Tr. at 342:23-25; 343:1-6.)

Q. Do you recall conversations, phone conversations with Mark Payton regarding Emily Downey?

A. I do.

Q. What was the substance of those calls?

A. Well, he called me to see what paperwork I would need to review Emily Downey's request to transfer her stock brokerage IRA account to a fixed annuity.

Q. And what did you do in response?

A. I gave Mark a list of forms that would need to be signed and/or completed.

(Hearing Tr. at 375:6-17.)

Of additional import here is the exclusive and symbiotic nature of Knowles' relationship with Payton. During the Department's direct examination of Payton the following testimony was elicited:

Q. What was your working relationship? How would you describe it?

A. Well, I was licensed to sell annuities, and Randy was licensed in the securities department, and we'd go on and do what I was licensed to do, talk to people about annuities and long term care, and Medicare supplements, and things of this nature. And if the discussion of securities came up in the client's home, I would contact Randy, and have him do all of the discussions concerning securities.

(Hearing Tr. at 271:20-25; 272:1-5.)

Q. Did you work with any other licensed securities person in Montana?

A. No.

(Hearing Tr. at 272:8-10.)

Each of these facts goes to the heart of the issue of "solicitation" and, therefore, the question of whether a suitability analysis was required. The lower court makes much of the fact that Knowles' expert witness articulated a clear explanation of the difference between trades that are solicited and those that are

not. (Dis. Ct. Order at 22.) However, Mr. Evanello[5] was not apprised of all the facts and was confused about the underlying facts. Mr. Evanello was unable to make a clear determination of whether the trades in question were solicited or not. (Hearing Tr. at 575:3-25; 583:1-23.) Additionally, the lower court's reference to the Change of Investment forms used to effect trades in Downey's investment account misses the fact that those forms were developed by and the property of FSC. Interestingly, the relevant testimony shows Payton actually filled out the form; Downey did not. (Hearing Tr. at 274:14-18.)

Knowles was relying on Payton to create new client prospects for Knowles and Payton relied on Knowles to liquidate securities portfolios to fund Payton's annuity sales. Their relationship was completely symbiotic, each needing the other in order to perform the business of taking money from senior citizens. The Commissioner was correct in his analysis resulting in the finding that Payton was Knowles' emissary. (Comm. C. Order at 19.) Knowles would never have had access to the accounts of these three senior women without Payton finding them, carrying Knowles' forms, and passing the securities business on to Knowles.

The United States Supreme Court long ago discussed the importance of the regulation of the securities industry:

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[5] The lower court refers to Knowles' expert as Jeffrey Evaillo, but his name is Evanello. T. Tr. at 542:19.

> A fundamental purpose, common to these statutes, was to substitute a philosophy of full disclosures for the philosophy of *caveat emptor* and thus to achieve a high standard of business ethics in the securities industry. As we recently said in a related context, 'It requires but little appreciation . . . of what happened in this country during the 1920's and 1930's to realize how essential it is that the highest ethical standards prevail' in every facet of the securities industry.

SEC v. Capital Gains Research Bureau, Inc., supra.

The lower court committed error and abused its discretion by deeming the Commissioner's Conclusion of Law 9 was clearly erroneous. The lower court completely ignored the import of the facts on the record regarding the various roles played by Knowles and Payton in their symbiotic relationship. The high standards of conduct required by the Montana Securities Act are rendered meaningless using the lower court's analysis of the facts and law in this case. The registration requirements and all that flows out from those requirements are negated by the lower court's analysis and subsequent reversal of the Commissioner's Corrected Order arriving at an absurd result.

ii. Solicitations of Securities Transactions Occurred in the Investors' Accounts.

The term "solicitation" is a term of art in the securities industry defined relative to the actions of the securities salesperson. If the salesperson does not suggest the securities transaction to his or her client, but rather the client suggests the transaction, such transaction is defined as "unsolicited." (Hearing Tr. at 57:9-13; 373:18-23; 341:5-16.) Knowles, as the registered securities salesperson, had a

strict duty to perform the proper analysis when recommending (soliciting) the purchase or sale of securities to a customer. (§ 30-10-201 (13) (g), MCA; ARM 6.10.126 (1) (c) and 6.10.126 (2) (f).)

In her testimony, the Department's expert witness, Ms. Lynne Egan, provided a lengthy description of why a suitability analysis is required and when it is required. Beginning on page 33 of the Hearing Transcript, Egan described the analysis required by law. (Hearing Tr. at 33:9-19.) Egan also testified how there can be very negative consequences if that analysis is not performed including potential tax consequences (Hearing Tr. at 34:17-18), additional charges for the sales of certain products (Hearing Tr. at 34:19-20) and other potential problems for the customer. (Hearing Tr. at 34:20-22.) Whenever securities transactions are solicited, a suitability analysis is required pursuant to § 30-10-201 (13) (g), MCA and ARM 6.10.126(1) (c) and 6.10.126(2) (f).

The administrative record includes reliable, probative and substantial testimony by the Department's expert, Egan, regarding the question of whether solicitations occurred and the consequence of those acts. After her qualification as an expert in regulation of the securities industry (Hearing Tr. at 27:13-25; 28:1-13), Egan testified that she had reviewed the FSC account statements of Emily Downey and Grace Simmons, as well as Doris Haaland. (Hearing Tr. at 51:19-21.) Egan testified that these statements indicate trades Knowles effected in those

accounts were not marked "unsolicited." (Hearing Tr. at 51:19-21; 54:1-5.) The account statements for Downey were entered into the record during her testimony. (Hearing Tr. at 141:3-21; Hearing Ex. 1 admt. at 134:17-25; Hearing Ex. 2 admt. at 141:3-21.) A review of these statements shows that certain trades are specifically marked as "unsolicited," such as those found on page three of the statement for the period of 11/30/2002-12/31/02. Of the six trades settled on 12/13/02, two of them are verified as "unsolicited." The remaining four trades are, therefore, "solicited." This fact is supported by the testimony of Egan, the Department's expert. (Hearing Tr. at 55:6-18.)

Simmons' account statements were entered into the record through Knowles in his direct testimony. (Hearing Tr. at 365:21-25; 366:1-15.) Egan also reviewed those and found similar "solicited" trading appearing in those statements. (Hearing Tr. at 51:19-21.) Because Haaland was deceased, her account statements were not entered into the record. Nonetheless, Egan testified that she reviewed all of the account statements. (Hearing Tr. at 51:19-21.) She also testified about the contents of those statements and what was indicated. (Hearing Tr. at 51:19-21; 55:4-18.) Knowles does not refute the fact that Egan reviewed the account statements of the alleged victims, nor does he refute that the statements reveal the trades he effected in those accounts were not identified as "unsolicited."

Pursuant to cross examination by Knowles' legal counsel, Egan testified that the marking of "unsolicited" on a trade ticket is carried through to the account statements and is "an affirmation of unsolicited. Otherwise, [the trade is] solicited." (Hearing Tr. at 55:16-18.) Egan testified under cross-examination that she also reviewed the trade tickets for these securities transactions, and "the information from the trade tickets flows through to the statement." (Hearing Tr. at 55:9-10.) Egan, again under cross examination, noted "[t]hat is the duty a broker has to do to affirm" whether a trade is unsolicited. (Hearing Tr. at 55:2-3.) Egan also testified that each individual security transaction requires a confirmation with regard to whether or not it is solicited. (Hearing Tr. at 57:12-13.) Finally, Egan noted in her most compelling testimony regarding the solicitation question that

> [t]he burden is on the broker dealer sales person (sic) at the time of the trade to mark the trade one way or the other. You can't mark it after the fact. If the trade was not marked unsolicited, it was solicited.

(Hearing Tr. at 59:25; 60:1-4.)

The findings of fact regarding solicitation of securities transactions are overwhelmingly important to this case because of Knowles' burden to conduct a suitability analysis for those solicited transactions. (§ 30-10-201 (13) (g), MCA; ARM 6.10.126 (1) (c) and 6.10.126 (2) (f).)

Whether the trades at issue were solicited is a fact question determined by testimony and documentary evidence in the record. This fact is addressed in the

Commissioner's findings, and these findings must be accorded deference. Further, the great weight of reliable, probative and substantial evidence on the whole record supports the Commissioner's findings of fact regarding Payton's role as Knowles' emissary and the Commissioner's findings of fact regarding the solicitation of securities transactions in the senior women's accounts.

The lower court erred and abused its discretion when it changed the Commissioner's findings that "the extent of Payton's actions as an emissary of Knowles was improper and in violation of Montana law" (Comm. C. Order at 19.) and then changed the Commissioner's finding as it is expressed in his Conclusion of Law 9 that "Payton acted as an emissary of Knowles . . . Payton solicited these securities transactions on behalf of Knowles . . ." (Comm. C. Order at 35; Conclusion of Law 9) to a new and completely contrary finding that "Payton did not actually effect or attempt to effect the sales of securities." (Dis. Ct. Order at 20-21.)

The lower court went into a lengthy recitation of the relevant parts of the Securities Act, including the definition of the term "transact." (Dis. Ct. Order at 19.) Pursuant to § 30-10-102 (24), MCA, the term "transact" includes the meanings of such industry specific terms as "sale," "sell," and "offer." Reading those definitions together it is clear that transacting securities business includes

soliciting the sale of securities for the purpose of purchasing annuity products with the proceeds of those securities sales.

Payton wanted to sell annuities and relied on Knowles to sell investors' securities to fund those purchases. As noted earlier, Knowles, as the registered securities salesperson had a strict duty to perform the proper suitability analysis when recommending the purchase or sale of securities to a customer.

However, Knowles did not perform the required analysis as set forth in the law for those trades that were solicited. His only explanation for this failure was that either the trades in question were unsolicited, (Hearing Tr. at 341:4-7 (Haaland), 373:18-19 (Simmons)) or the review was limited to two transactions (383:18-24 (Downey)) contrary to the substantial credible evidence found on the record reviewed in its entirety. A review of certain of the securities transactions effected by Knowles in the accounts held by Simmons shows they were solicited and required a suitability analysis. (Hearing Ex. I admt. at 344:1-12; Hearing Ex. L admt. at 354:16-20; Hearing Ex. M admt. at 356:2-25; 357; 358:1-10; Hearing Ex. N admt. at 359:5-14; and Hearing Ex. O admt. at 366:11-17.) A review of Downey's account shows more than just the two transactions were solicited. (Hearing Ex. 1 and 2.) Again, applying the substantial credible evidence (facts) to the law, no other conclusion of law can be reached than that Knowles violated the Montana Securities Act by his failure to perform the required suitability analysis

based on the substantial credible evidence found pursuant to a review of the entire record.

iii. Knowles Attempted to Effect a Securities Transaction While Not Properly Licensed.

Later in its Order, the district court indicates the Commissioner's Finding of Fact numbered "35" "is incomplete based upon the record." (Dis. Ct. Order at 24.) The court seems to contradict itself where it states "Knowles did not make any representation about his association with a broker dealer. (Trans. at 318.)" and then states ". . . Knowles testified that he told the Johnsons that he was in between broker-dealers . . ." (Trans. at 318.) and "[a]ccording to Kaye Johnson, Knowles told her that he was between brokers and was going to change companies and that Knowles told her that Rolshoven was his supervisor (Trans. at 180-182.)." (Dis. Ct. Order at 24.) The court, in an abuse of its discretion, modified the Commissioner's Finding of Fact 35 apparently adding these contradictory facts. (Dis. Ct. Order at 24.) The lower court also adds facts to the Commissioner's Finding of Fact 37, acting in error and in an abuse of its discretion. The lower court makes several similar modifications to the Commissioner's Findings of Fact, adding what the court deems as omitted facts. (Dis. Ct. Order at 24-25.) Each of these modifications represents error committed by the court and an abuse of its discretion.

Perhaps more disturbing, the lower court again altered the Commissioner's Findings of Fact by indicating "Knowles did not make any offer, sale, or purchase of a security for Johnsons." (Dis. Ct. Order at 25.) The court goes on to change the Commissioner's Finding of Fact 39 to read the opposite of the Commissioner's finding, indicating Knowles' actions with the Johnsons "did not constitute an attempt to effectuate a securities transaction . . . ." (Dis. Ct. Order at 26-27.)

The Department's expert, Egan, testified regarding the important role registration of securities salespersons plays:

Q. Why do we [State of Montana, Securities Department] ask people to be registered as a securities sales person?

A. Well, one of our primary purposes under the purposes section of the [Montana] Securities Act is to protect the investor. . . . investors can place trust in sales persons . . . we want the individual or individuals that are assisting people in the management of their money to have the requisite knowledge and skills, and know the law in order to do business in this state.

And that's why registration is required, because registration encompasses testing, continuing education, and a continuing license requirement to ensure that that person is of the proper caliber to do business in the state.

(Hearing Tr. at 30:11-25, 31:1.)

Knowles knew this and says so in his own testimony.

Q. (by Ms. Cross Guns) How does a person become licensed and registered to be a securities sales person?

A. You are sponsored by a broker dealer, you take the Series 7 exam and other exams.

(Hearing Tr. at 409:12-16.)

Q. If that sponsorship ends, you're saying that your license is still valid?

A. Yes. You don't have to –

Q. You can continue to conduct securities sales person business?

A. No.

(Hearing Tr. at 410:10-15.)

Q. So that means that you cannot conduct broker dealer sales person activities?

A. That's correct.

(Hearing Tr. at 410:21-23.)

Knowles' former supervisor, Eric Rolshoven, testified during redirect examination that Knowles was attempting to effect a securities transaction when he took Johnson's check for deposit into her IRA account. (Hearing Tr. at 252:3-15.)

The Commissioner correctly indicates in his order that "[t]he Hearing examiner, who was able to observe the witnesses, found Kaye Johnson's testimony to be more credible than Knowles' testimony with regard to [Findings of Fact #34 and #35]. The Commissioner will defer to the Hearing Examiner's determination with regard to the credibility of the witnesses on these points." (Comm. Ct. Order at 30, Footnote 18.) Error is committed where the court substitutes its judgment with regard to the weight given the evidence by the agency, and error is committed where the entire record is not reviewed. (§ 2-4-704 (2), MCA.) ***Brackman,*** supra**.**

The lower court lacked authority to alter or augment the findings of fact in the Commissioner's Corrected Order and then compounded its error by ignoring the great weight of evidence supporting the Commissioner's Corrected Order. The lower court abused its discretion here.

II. THE LOWER COURT'S FAILURE TO GIVE THE REQUIRED DEFERENCE TO THE DEPARTMENT'S FINDINGS OF FACT AND ITS INTERPRETATIONS OF ITS RULES IS AN ABUSE OF DISCRETION.

The lower court erred by not viewing the agency's findings of fact in the light most favorable to the agency. The lower court further erred by failing to give great weight to the agency's interpretations of its own rules.

A. Standard of Review

This Court has long held that "[t]he reviewing court must view the agency's findings of fact in the light most favorable to the agency." ***Harding v. Savoy***, 2004 MT 280, & 20, 323 Mont. 261, 100 P.3d 976; ***Peschel Family Trust v. Colonna***, 2003 MT 216, & 19, 317 Mont. 127, 75 P.3d 793. The ***Peschel*** Court additionally noted that "[i]t is not a matter of whether this Court agrees with the [agency's] findings and conclusions." ***Peschel*** at & 19. A reviewing court "'may not substitute its judgment' for the agency's 'as to the weight of the evidence on questions of fact.'" (§ 2-4-704(2), MCA.) ; ***Benjamin v. Anderson***, supra.

Additionally, in ***Brady v. Mont. DOJ***, 1999 MT 153, 295 Mont. 75, 983 P.2d 292, this Court reiterated its longstanding position that a state agency's interpretation of its own rules should be given great deference.

> The agency's interpretation of its rule is afforded great weight, and the court should defer to that interpretation unless it is "plainly inconsistent" with the spirit of the rule. The agency's interpretation of the rule will be sustained so long as it lies within the range of reasonable interpretation permitted by the wording.

Brady at & 22.

B. Discussion

Despite these clear mandates, the court altered the findings of fact to remove them from the light most favorable to the agency. The court did not give the agency the deference with regard to findings of fact as required by law, both case law and statutory law. (§ 2-4-704, MCA.); ***Harding***, ***Peschel***, ***Benjamin***, and ***Brady***, supra.

i. Solicitation and the Use of an Emissary

On page 22 of the District Court Order, the court says the "record is clear and unrefuted that the clients initiated the contact with [Mark] Payton seeking information regarding annuities." (Dis. Ct. at 22.) Rather, the record is clear that Payton hired a service to send cards to these people as a means of finding new customers. Furthermore, while Payton responded to those inquiries regarding annuities, he took the next step of getting involved in their securities portfolios by

introducing Knowles into the transactions. Of great import here is the testimony provided by Knowles' former supervisor, Eric Rolshoven. Rolshoven indicated only Knowles could present the forms to securities customers that Payton was using as Knowles' emissary. (Hearing Tr. at 228:25; 229:1-25; 230:1-19.)

In testimony provided by the Department's expert, Egan, the following interpretation of the laws and rules administered by the Department is given:

> It is my opinion that . . . Mr. Knowles liquidated [securities positions held by the victims] without doing an adequate reasonable inquiry into the investor's financial objectives, to determine whether or not it was in the client's best interests based on age, level of sophistication, level of securities experience, net worth, liquid net worth, liquidity needs, capital consequences – (inaudible) – sales charge consequences.
>
> (Hearing Tr. at 47:17; 48:13-20.)

The Commissioner's order presents a lengthy discussion of the hearing examiner's findings of fact regarding Payton's relationship to Knowles and how that relationship was unlawful pursuant to the Montana Securities Act. While the lower court may wish to insert additional findings, it may not do so. Furthermore, the reviewing court "may not substitute its judgment" for that of the agency. (§ 2-4-704 (2), MCA.) ***Peschel***, supra., Once the lower court altered the findings of fact, it was no longer reviewing the facts in the light most favorable to the agency. Thus, not only was the altering of the findings of fact in error, the failure to review those facts in the light most favorable to the agency was an abuse of the lower

court's discretion. (§ 2-4-704, MCA.) ***Harding***, ***Peschel***, ***Benjamin***, and ***Brady***, supra.,

In the end, the lower court abused its discretion when it failed to afford the weight due the Department's interpretation of its laws and rules with regard to whether Knowles could utilize an emissary to solicit securities transactions, and with regard to what constitutes a solicited transaction.

ii. Discussion Relevant to Kaye Johnson

The district court erred and abused its discretion by misapprehending the significance of the facts surrounding Knowles' representation that he was "between firms." One cannot be "between firms" and maintain proper registration and licensure as a securities salesperson or an investment advisor representative. (§ 30-10-201, MCA.)

Egan and Knowles both provided reliable, probative and substantial evidence that a securities salesperson cannot be "between firms." (See Argument I, Discussion iii.) A person who is between firms cannot transact securities business because his or her registration relies on the sponsorship of a broker-dealer firm.

As noted above, Knowles' former supervisor, Eric Rolshoven, testified during redirect examination that Knowles was attempting to effect a securities

transaction when he took Johnson's check for deposit into her IRA account. (Hearing Tr. at 252:3-15.)

Again, there is a great weight of reliable, probative and substantial evidence on the whole record supporting the Commissioner's Corrected Order. As noted above, once the court altered the findings of fact, it no longer reviewed them in the light most favorable to the agency. Thus, not only was the altering of the findings of fact in error, the failure to review those facts in the light most favorable to the agency was error and abuse of discretion.

Also, as noted above, the lower court again altered the Commissioner's findings of fact by indicating that "Knowles did not make any offer, sale, or purchase of a security for Johnsons." (Dis. Ct. Order at 25.) The court goes on to change the Commissioner's Finding of Fact 39 to read the opposite of the Commissioner's finding indicating Knowles' actions with the Johnsons "did not constitute an attempt to effectuate a securities transaction . . . ." (Dis. Ct. Order at 26-27.)

The lower court abused its discretion when it failed to afford the weight due the Department's interpretation of its laws and rules with regard to whether Knowles transacted securities business with Johnson. In testimony provided by the Department's expert, Egan, the following interpretation of the laws and rules enforced by the Department is given:

> It is my expert opinion that Mr. Knowles transacted securities business with Kaye Johnson when he went to her home in October or November of 2004; and through his long term relationship with her, led her to believe he was still with FSC; he discussed her investments; he discussed purchasing the Franklin AGE income fund; and he received a $3,500 check directly from her for her IRA; and through that, he acted as an unregistered sales person . . .

(Hearing Tr. at 49:15-24.)

The agency's interpretation of the laws and rules it administers must be given deference. This court erred when it failed to afford the weight due the Department's interpretation of its laws and rules with regard to whether Knowles was conducting securities business in violation of the law in his conduct with Emily Downey, Grace Simmons, and Kaye Johnson.

CONCLUSION

The lower court erred and abused its discretion when it reversed the Commissioner's final agency decision. The lower court abused its discretion by altering the Commissioner's findings of fact. The court abused its discretion by failing to review the facts in a light most favorable to the agency. The court abused its discretion by failing to give deference to the agency's interpretation of its laws and rules.

The high standards of conduct required by the Montana Securities Act are rendered meaningless using the lower court's analysis of the facts and law in this case. The registration requirements and all that flows out from those requirements

are negated by the lower court's analysis and subsequent reversal of the Commissioner's Corrected Order, arriving at an absurd result.

DATED this 19th day of March, 2008.

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CERTIFICATE OF SERVICE

I hereby certify that I have filed a true and accurate copy of the foregoing Brief of Appellant with the Clerk of the Montana Supreme Court and that I have served true and accurate copies of the foregoing upon each attorney of record and each party not represented by an attorney in the above-referenced appeal, as follows:

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